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No. 82-2091

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

SHEARN MOODY, JR.,
Petitioner,

v.

DAVID C. MEYERS, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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REPLY BRIEF FOR PETITIONER

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In our petition, we took the position that the courts below improperly chose to substitute their judgment regarding valuation of insurance-company assets for the judgment of a state insurance commissioner. Petition at 8-18. In addition, we noted that the court of appeals wrongly imposed a rule of its own making to govern a state-law claim rather than identifying and adhering to state law. Petition at 18-23. Respondents offer little or no answer to these points, largely choosing to argue that the facts support the judgment below.[1] We make the following points in reply.

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[1] In presenting their version of the facts, respondents rely far more on rhetoric than on citation to the record. See Brief in Opp. at 4-6. Contrary to their assertions, petitioner did present substantial evidence regarding the issue of the valuation, including testi-

1. Mindful that this Court does not sit to review questions of fact, respondents claim that our petition seeks merely to challenge findings of fact by the jury. That argument completely misses the point. Our position is not that the jury incorrectly decided the issue of valuation but that it should not have been allowed to decide the issue at all. The valuation of insurance-company assets is not the business of a federal court. See Petition at 8-18.

It does not improve respondents' argument to salt it with claims that the valuation was rendered ignorantly or as the result of misconduct. To begin with, it is well-established that such allegations are insufficient to justify collateral attacks on agency determinations. See, e.g., *Bolton* v. *Coats*, 514 S.W.2d 482 (Tex. Civ. App. 1974); *Jay* v. *State*, 15 Ala. App. 255, 73 So. 137 (1916). See also *Providence Rubber Co.* v. *Goodyear*, 76 U.S. (9 Wall.) 788 (1870). Moreover, an exception of this sort would make formal state action meaningless whenever a plaintiff could offer belated testimony suggesting that the state officials were misinformed. As this Court said only a few years ago, in discounting testimony from state officials that agency approvals had been given " 'unwittingly' or only because the departments were unfamiliar at the time" with particular types of agreements: "[W]e do not think this after-the-fact testimony from single officials should outweigh the formal, official approval rendered under the names of the commissioners after opportunity for full review." *United States* v. *Consumer Life Insurance Co.*, 430 U.S. 725, 751 n.36 (1977).[2]

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mony from Empire officials and Frank Ussery, an Alabama Commissioner of Insurance. See, e.g., T. 1427-97, 1573-1617. Moreover, as we discuss below, their charges of "fraud" depend on the predicate that the trust was overvalued, a predicate that assumes the propriety of having a federal jury make its own after-the-fact determination of the trust value. Our petition, of course, is based on the belief that such an assumption is wrong as a matter of law.

[2] The Court also noted that "this formal approval withstood careful triennial audits." *Id.* at 751 n.36.

This case would be a particularly inopportune one in which to invent a contrary rule. Here, the only misconduct alleged, in respondents' own words, is "allowing an under capitalized life insurance company to embark upon an aquisition [sic] program by virtue of a paper surplus of $14 million established without appraisal or verification when Empire was receiving between $165,000 to $250,000 income from the trust and did not have true surplus asset resources with which to withstand the risk of such growth and attendent [sic] expenses." Brief in Opp. at 5. But the questions whether Empire was "undercapitalized" or had a "paper surplus" are precisely the questions that were before the Commissioner when he decided to value the trust asset at the $14.2 million figure. If the determination of the Commissioner is deemed controlling, as we submit that it should be, then the claims of undercapitalization and the like disappear by their own hypothesis.[3]

Whatever respondents might prefer, an improper failure to abstain cannot be excused by touting the ultimate decision on the merits. It is possible, of course, that a federal judge or jury may have a surer feel for the value of a reserve asset than a state insurance commissioner, just as they might make a better judgment about the propriety of a drilling order (*Burford* v. *Sun Oil Co.*, 319 U.S. 315 (1943)), or the need for continuing railway service (*Alabama Public Service Commission* v. *Southern Ry. Co.*, 341 U.S. 341 (1951)), or the reasonableness of automobile insurance rates (*Allstate Insurance Co.* v. *Sabbagh*, 603 F.2d 228 (1st Cir. 1979)), or the merits of an exclusionary clause in an insurance policy (*Smith* v. *Metropolitan Property & Liability Ins.*, 629 F.2d 757 (2nd Cir. 1980)). But the likelihood is sufficiently low,

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[3] Not even respondents have suggested that the raw figures submitted to the Commissioner were in any way inaccurate. Their complaint is simply that, based on those figures, a value of $14.2 million was excessive. Brief in Opp. at 5.

and the intrusion on state regulation sufficiently grave, that this Court and various courts of appeals have required the federal courts to abstain. The same course should have been followed here.[4]

2. Apparently seeking to evade both the abstention and federal-common-law arguments, respondents assert that "[t]here was no evidence of any 'valuation' made by the State of Alabama." Brief in Opp. at 5. The assertion is demonstrably false.

First, the law is unequivocal on this point. In 1965, when the valuation of $14.2 million was set, Alabama law provided that "[t]he superintendent of insurance [later called the Commissioner] shall allow to the credit of an insurance company, in the account of its financial condition, on such assets as are or can be made available for the payment of losses in Alabama." 28 Ala. Code § 61 (1959). When the Code was revised in 1971, the Commissioner was similarly charged to admit "[o]ther assets, not inconsistent with the provisions of this section, deemed by the commissioner to be available for the payment of losses and claims, at values to be determined by

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[4] Although respondents stress that "the plaintiff in this action was the Alabama Commissioner of Insurance," Brief in Opp. at 8, they neglect the nominal nature of his appearance. This omission is particularly noteworthy because, in the district court and court of appeals, respondents took exactly the opposite position. For example, counsel for the Receiver insisted at trial: "I do not represent the Department of Insurance of Alabama." T. 78. Similarly, on appeal, respondents declared: "When Moody increased the value of the Trust and sought approval from the Insurance Commissioner of Alabama, he was dealing with a state regulatory agency, whose responsibility was to the insurance public, however in the instant case, as receiver of Empire he is for all purposes and intent the corporation itself. See *Carpenter* v. *Pink*, 124 S.W.2d 981 (Tex. 1939). *The instant lawsuit thus is brought not by the Insurance Commissioner, but by the corporation on behalf of its creditors, stockholders and policyholders. Cotton* v. *Republic National Bank of Dallas*, 395 S.W.2d 930 (Tex. 1965)." Appellees' Brief at 64 (emphasis added). Their current position thus has proved unpersuasive even to themselves.

him." Ala. Code § 27-31-1 (13) (1977). Under either provision, it is evident that the Commissioner must ultimately decide whether an asset is "available for the payment of losses" and, if so, in what amount.

Second, the record in this case leaves little doubt that the Alabama Commissioners actively exercised that power. In 1965, for example, when Empire submitted a letter from an actuary showing a range of values (as of December 31, 1964) from $7,795,200 to $14,403,200 to $29,499,200, DX 64, the Alabama Commissioner declined to accept the higher figure and, in fact, reduced the middle figure by approximately $200,000 to the admitted value of $14,213,440.[5] The Empire Examination Report (on which respondents seek to rely (Brief in Opp. at 7, n.3) likewise notes that, in the following year, a "decision was given by the Superintendent of Insurance of the State of Alabama" allowing the value to be carried at $14,213,440 subject to requirements about insurance and collateral. DX 6, at 57. The Examination Report then directed creation of a liability account under the title "Security Valuation Reserve" that effectively lowered the net value of the trust asset to $13,528,000. In 1968, Commissioner Ussery, according to his own testimony, independently decided upon a requirement that Empire establish a reserve account, to be increased by $430,000 a year, to reflect the declining value of the life interest as the life tenant grew older. T. 1583-1586. Finally, in 1972 Commissioner Bookout required the trust interest to be carried at a value of $4,250,000. This course of events hardly reflects a passive role for the state Commissioner.[6]

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[5] As we noted in our Petition (at 3 n.3), the court of appeals gives the mistaken impression that the Commissioner reflexively accepted a figure submitted by the company. In fact, the Commissioner settled upon his own figure, an amount somewhat less than the second highest number submitted by the company.

[6] In light of this direct involvement in the setting of valuation figures, respondents' analogy to a SEC filing is off the mark. See Brief in Opp. at 8.

Third, we note that respondents contradict their own argument. For, while deprecating the authority of the Commissioner in one breath, at the same time they insist upon the finality of his valuation in 1972 that led to Empire's insolvency. Brief in Opp., at 9-10. As respondents appear to admit, it would have been wholly improper for Empire to have carried the trust interest at $14,213,440 after the Commissioner had held its value to be $4,250,000. It would have been equally improper for Empire (or petitioner) to have gone to federal court to seek a higher valuation or to hold the Commissioner liable for the resulting insolvency. The correctness of such determinations is not a matter for federal interference, an observation that applies to the 1965 valuation as well as to the 1972 one.[7]

3. It is an oddity of respondents' brief that, while belaboring points not raised in our petition (e.g. equitable estoppel), see Brief in Opp. at 6-9, it is virtually mute on issues that were raised. Respondents thus address the issue of abstention only indirectly and the issue of federal common law not at all. We think their silence merits further attention.

The basic issue here is whether a federal court or a state official should make the controlling decision regarding valuation of assets held by insurance companies. At trial, respondents took the position that "the approval of the Department has no relevancy" (T. 1582), a position that they seem to track in the Brief in Opposition. Brief in Opp. at 7-8. Yet, if that position were accepted, the decisions of state insurance regulators would be routinely voidable whenever a federal court, often acting on

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[7] Although respondents note that petitioner did not appeal the 1972 determination, which caused the company to become insolvent, Brief in Opp. at 9-10, that argument is a red herring. Petitioner is not contending that the federal court should have overturned the 1972 valuation; rather, he is saying that it should not have overturned the 1965 one. See Petition at 11.

the basis of hindsight, reached a different conclusion.[8] Even if that were a desirable result, which it is not, it would mark a radical change in the states' authority over insurance matters. See 15 U.S.C. § 1011 ("the continued regulation and taxation by the several states of the business of insurance is in the public interest").

It is not surprising, therefore, that respondents cite no cases allowing the federal courts to embrace collateral attacks on state insurance decisions. Nor do respondents even explain why it would be a good idea. If Alabama courts wish to recognize such a cause of action, aggrieved persons will be able to obtain all appropriate relief without the interference of a federal court. On the other hand, should the Alabama courts hold that such collateral attacks are impermissible, then it would be especially inappropriate for the federal courts to exact damages on the ground that state determinations were erroneous. See *Construction Aggregates Corp.* v. *Rivera de Vicenty*, 573 F.2d 86, 96 (1st Cir. 1978) (federal court, sitting in diversity, cannot entertain cause of action not recognized under state law). The role of the federal courts is, at best, superfluous, and, at worst, distorting.

Respondents also present no real defense of the inclination of the court of appeals to fashion federal common law. Although respondents do suggest that state law denies the Commissioner final authority over valuation of insurance assets, that suggestion is plainly wrong (see pages 4-5, *supra*) and, in any event, is unresponsive to the problem. Even if we concede that federal common law at times may fortuitously coincide with state law, it is the responsibility of the federal courts to seek out state

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[8] The importance of hindsight is not merely theoretical. In this case, for example, the court of appeals relied on the earnings history of American National Insurance Co. (the principal trust asset) *after 1965*. Pet. App. at A-22. The Alabama Commissioner obviously could not have considered that information in making the 1965 determination.

law directly, not to rely on the law of averages. The failure to do so is a serious concern in any case, regardless of the actual result. When, as here, the federal rule reverses state law, the affront to *Erie* principles is even more severe.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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